

October 15, 2010

GLORIA L. FRANKLIN, CLERK

U.S. BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

IT IS SO ORDERED.

Signed 10-13-2010
ROGER L. EFREMSKY
U.S. Bankruptcy JudgeUNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re

AVON TOWNHOMES VENTURE,

Debtor.

Case No. 05-53243-RLE

Chapter 7

**MEMORANDUM DECISION RE ORDER TO DISGORGE COMMISSION RECEIVED
BY JAMES MCCLENAHAN AND EAGLE HOME LOANS**

On July 30, 2010, the Court issued its Memorandum Decision Regarding Court's Order to Show Cause ("Memorandum Decision") and Order Pursuant to Memorandum Decision ("Order"). The Order directed James McClenahan ("McClenahan") and/or Eagle Home Loans, Inc. ("Eagle Home Loans") to file a written response to the Court's tentative decision to order McClenahan and Eagle Home Loans to disgorge \$18,300 in commission received as a result of the sale of a parcel of partially developed real property in Lathrop, California (the "Property"). McClenahan timely filed his Response To Tentative Decision on August 30, 2010, which also included a Motion To Amend/Clarify Findings (the "Response").

The following constitutes the Court's Findings of Fact and Conclusions of Law, pursuant

1 to Rule 7052 of the Federal Rules of Bankruptcy Procedure. In addition, the Findings of Fact and
2 Conclusions of Law in the Court's Memorandum Decision is incorporated by reference herein.

3 4 **I. FACTUAL BACKGROUND**

5 A detailed discussion of the factual and procedural background can be found in the
6 Court's Memorandum Decision. Nevertheless, the Court shall provide a summary of the relevant
7 facts as it pertains to McClenahan and Eagle Home Loans.

8 On May 15, 2008, the Court issued an Order to Show Cause directing various parties,
9 including McClenahan, to appear in Court and show cause why sanctions should not be imposed,
10 individually and/or jointly, for their conduct regarding the sale of the Property. On October 7,
11 2008, after four days of evidentiary hearings, the Court issued an Amended Order to Show Cause
12 directed at Stanley A. Zlotoff, as Debtor's counsel, and Joe Guerra, as Debtor's Responsible
13 Individual. Thereafter, the Court conducted additional evidentiary hearings.

14 After the conclusion of the evidentiary hearings, the Court determined that McClenahan¹
15 acted as the broker on behalf of the Debtor in the sale of the Property and received commission in
16 the amount of \$18,300 (the "Commission") as a result of the sale. See Memorandum Decision,
17 pp. 60:18 - 62:14. However, neither Eagle Home Loans nor McClenahan was employed by the
18 Debtor with the Court's approval.

19 As a result, although the Court did not sanction McClenahan under its inherent powers,
20 the Court tentatively held that because McClenahan's employment was not authorized by the
21 Court, the receipt of the Commission was improper and must be disgorged. Because the Order to
22 Show Cause only warned McClenahan of the possibility of sanctions generally pursuant to 11
23 U.S.C. § 105 and not disgorgement under 11 U.S.C. § 327, the Court gave McClenahan an
24 opportunity to respond in writing.

25 McClenahan filed his Response on August 30, 2010, which included a Motion to

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27 ¹ McClenahan testified that he is the president, CEO and 100% shareholder of Eagle Home Loans, Inc. See 7/25/08
28 Transcript, Docket #269, at 24:18-25:1; 10/6/08 Transcript, Docket #289, at 77:3-24. Thus, for purposes of this
Memorandum, the terms "McClenahan" and "Eagle Home Loans" are used interchangeably.

1 Amend/Clarify Findings in the same pleading.

2 3 **II. DISCUSSION**

4 As stated in the Memorandum Decision, section 327 of the Bankruptcy Code permits the
5 trustee, with the approval of the court, to employ attorneys, accountants and other such
6 “professional persons,” provided such professionals “do not hold or represent an interest adverse
7 to the estate” and are “disinterested persons.” 11 U.S.C. § 327(a). Section 327 applies to debtors
8 in possession by virtue of § 1107(a).

9 A real estate broker is a “professional person” as contemplated by § 327. In re Silver Oak
10 Homes, Ltd., 167 B.R. 389, 398 (Bankr. D.Md. 1994); In re McConnell, 82 B.R. 43, 44 (Bankr.
11 S.D. Tex. 1987); In re Eastern Inns of New Hampshire, Inc., 72 B.R. 418, 420 (Bankr. D. Me.
12 1987); In re Roberts, 58 B.R. 65, 67 (Bankr. D.N.J. 1986). A real estate broker is not entitled to
13 a commission on the sale of estate property where his employment was not approved by the
14 bankruptcy court. In re Haley, 950 F.2d 588, 590 (9th Cir. 1991); Enea v. Coldwell Banker/Del
15 Monte Realty, 225 B.R. 715, 719 (N.D. Cal. 1998). “The purpose of section 327 requiring prior
16 court authorization of a professional’s appointment is to eliminate volunteerism and aid the court
17 in controlling estate administrative expenses.” Haley, 950 F.2d at 590 [citations omitted].

18 The law is well-settled that “[f]ailure to receive court approval for the employment of a
19 professional in accordance with § 327 and Rule 2014 precludes the payment of fees.” DeRonde
20 v. Shirley (In re Shirley), 134 B.R. 940, 944 (9th Cir. 1992); Atkins v. Wain, Samuel & Co. (In re
21 Atkins), 69 F.3d 970, 973 (9th Cir. 1995)(“In bankruptcy proceedings, professionals who perform
22 services for a debtor in possession cannot recover fees for services rendered to the estate unless
23 those services have been previously authorized by a court order.” [citations omitted]).

24 McClenahan’s Response does not dispute that neither he nor Eagle Home Loans obtained
25 the Court’s authorization to be employed as broker for the Debtor. The Response also does not
26 dispute the Court’s finding that McClenahan and/or Eagle Home Loans acted as the broker on
27 behalf of the Debtor. Instead, McClenahan appears to argue, without any supporting legal
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1 authorities, that disgorgement would be improper because the Commission was earned and the
2 estate received the benefit of the sale. However, “[a]s a general rule the equitable remedy of
3 quantum meruit cannot be available where the fees are barred by law under the bankruptcy
4 rules.” Halperin v. Occidental Financial Group, Inc. (In re Occidental Financial Group, Inc.), 40
5 F.3d 1059, 1063 (9th Cir. 1994). Otherwise, any unapproved professional could assert an
6 equitable claim to compensation.

7 The fact that McClenahan or Eagle Home Loans paid \$18,000 of the Commission to
8 Debtor’s counsel out of his own volition does not change the basis of the disgorgement. To
9 accept McClenahan’s suggestion that the Court direct the disgorgement order to Debtor’s counsel
10 would mean that any professional who is ordered to disgorge fees could simply assert that he
11 spent the fees in question and the Court must track down the recipients of the funds. The Court
12 is under no such obligation.

13 Likewise, it is irrelevant whether it was McClenahan or Eagle Home Loans who actually
14 received the Commission. Neither of them was employed with the approval of the Court. Since
15 McClenahan is the President, CEO, and 100% shareholder of Eagle Home Loans, the
16 disgorgement is properly directed to him.

17 McClenahan placed much emphasis on the fact that the Order on Motion to Sell Property
18 Free and Clear allowed for the payment of a realtor’s commission. Contrary to McClenahan’s
19 assertion, an order allowing payment of a commission from sale proceeds, along with payments
20 of other fees and liens, is not synonymous with the approval of a professional’s employment or a
21 professional’s compensation, which is governed by 11 U.S.C. §§ 327-330. Indeed, unless
22 ordered otherwise, a professional employed by a debtor must submit a fee application seeking
23 court approval of its fees, and a bankruptcy court has a duty to review said fee application
24 notwithstanding the absence of objections by the trustee, debtor or creditors. See Lobel & Opera
25 v. United States Trustee (In re Auto Parts Club, Inc.), 211 B.R. 29, 33 (9th Cir. BAP 1997).

26 Lastly, McClenahan’s arguments and legal authorities pertaining to the due process
27 requirement of sanctions are inapplicable in this instance. As stated in the Memorandum
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1 Decision, the Court held that sanctions under the Court's inherent powers against McClenahan
2 were inappropriate. See Memorandum Decision p. 60:3-4. The statutory predicate for the
3 disgorgement of the Commission is 11 U.S.C. § 327 and its related case law.

4 Mindful of due process concerns, the Court gave McClenahan thirty (30) days to respond
5 to the proposed disgorgement. McClenahan contends that had he known of the possibility of
6 disgorgement, he would have examined the witnesses differently at the evidentiary hearings.
7 However, any additional testimony from Carlos Hernandez or Debtor's counsel would not alter
8 the fact that neither McClenahan nor Eagle Home Loans were or was employed pursuant to court
9 authorization, which McClenahan did not dispute. Furthermore, as the Court clearly stated in its
10 Memorandum Decision that the basis of the disgorgement was the failure to obtain court
11 approval for employment, McClenahan was free to provide declarations and legal authorities to
12 show why the Commission should not be disgorged despite his failure to obtain court approval of
13 employment. He did not do so.

14 In sum, McClenahan has not provided the Court with any reasons or cited any legal
15 authorities to support his position that he is entitled to the Commission despite his failure to
16 obtain employment authorization. Based on the foregoing, the Court finds that McClenahan and
17 Eagle Home Loans failed to obtain court approval for their employment as broker for the Debtor
18 in accordance with 11 U.S.C. § 327 and thus they are not entitled to the Commission in the
19 amount of \$18,300 for the sale of the Property. The Commission shall be disgorged to the
20 Chapter 7 Trustee.

21 With regard to the Motion to Amend/Clarify Findings ("Motion"), McClenahan did not
22 provide appropriate notice and opportunity for hearing of the Motion to the other interested
23 parties, as required by Federal Rule of Bankruptcy Procedure 9014 and Local Bankruptcy Rule
24 9014-1. Therefore, the Motion will be denied without prejudice.

25 An appropriate Order shall issue.
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